A 'Learnings' Report from my Family Business consulting experience.....

A Primer on Family Business

By Raju Swamy (Version – 8) (Original Version published in March 17, 2009/ Updated on November 05, 2018) (9 pages)

An introduction to typical issues confronting Family-owned and managed business enterprises and suggestions on how we can resolve them ….

Raju Swamy
Founder & Advisor to Family Business
PROMAG Consultancy Services
Bangalore - 560004
Tel. +91-80-26676298/ Cell: 9845271498
rajupromag@hotmail.com/ www.promagconsult.in
Strengthening Family Dynamics for Family Business Growth....
....since 1985

I have been consulting to Family Business Clients – in different business sectors and locations - for over 33 years and each time I have consulted with a new Family Business my appreciation and understanding of the dynamics of Family and Business and Business and Family multiplied significantly. Factual exposure combined with intuitive reasoning, based on productive experience in the face of one-of-kind-challenges, kindled a passion that has made me obsessively interested in consulting only to Family Businesses.

Added assets to my learning have been the fact that prior to my consulting career I worked for over 18 years with a very reputed family-promoted but professionally run Business Group in the Automobile Components Industry. I joined them as a Management Trainee soon after passing out with an MBA from the first batch of IIMC (IIM Calcutta), in 1966. My career spanned Marketing, Sales, Projects, HR, and I was Country Head of Marketing for the entire Group at the time of leaving in 1983. I also worked very closely with the Group Chairman in the New Projects and HR areas.

This article represents my broad understanding of prevailing Family Business dynamics particularly true of Indian and Asian Family Businesses. I keep making revisions as I discover something new and the current one – Version 8 – was updated very recently.

World-wide, the commonly held belief is that atleast 70 per cent of Business Enterprises are Family-owned or Family-promoted…..in India the percentage may be nearing 80 per cent, including Small, Medium, and Large enterprises. Again, experience across the World shows that Family Businesses generally progress to the second generation, but, only a very optimistic 30 per cent or less manage to survive through and beyond the third generation. The obvious reason is that education, exposure, living standards, aspirations multiply in succeeding generations and if a particular Family Business has not kept pace with product, market, and industry relevance, with growth requirements and with aspirations of a more demanding generation, succession becomes a hurdle resulting in the Family Business struggling to survive.

Additional issues related to Succession and longevity of Family Business include the declining percentage of younger generation in the population profile in most of the traditionally industrial nations of Europe. In the USA, Succession issues in many Family Businesses arise from the complexities of accommodating children born of multiple marriages. This could be true in some cases in Europe too.

My awareness about issues of Family Business has also been enhanced to a very large extent by my ‘in person’ learning exposure to Prof. John Ward during his presentations and debates at the Confederation of Indian Industry’s Annual Family Business Conventions for nearly 15 years between 2000 and I think 2014. Prof. Ward is considered a leading authority on Family Business

Governance. His case study on the Murugappa Group is a ‘classic’ in Indian Family Business studies, and it is still one of a kind.

I now come down to my interpretation on the Family Business environment in India.

From the 1990s, Family Business issues have become particularly important given the need to compete, survive, and grow in a liberal ‘survival of the fittest’ business climate coupled with an increasingly demanding internal family environment.

Traditionally, in a less high pressure business environment, most small and medium family-owned and owner-managed businesses have been living with their problems either on grounds of protecting ‘family prestige’ or simply because of a feeling of helplessness in a closed hierarchical society.

However, trends can be noticed In the case of most of the relatively ‘medium-to-larger’ closely-held family managed businesses with recognizable brand equity that have emerged over the last 50 years and more. Most of my clients fall in this category….at least two of them are over 100 years old. All of them have been ‘founder-managed’ or single family managed, to start with.

With the traditional hierarchy of the single family in place (father and unmarried sons / elder brother and younger brothers) and with a good business performance and cash flow, and mutual understanding, peace has prevailed. In most such enterprises, and particularly where manufacturing, and international business and trading are involved, the ‘family managers’ are well educated and business-competitive. Work and responsibility are shared informally with mutual understanding.

Over time, however, with the business track record being good, and with relative peace and mutual understanding within the family, complacency on the family front sets in.

Mutual understanding is taken for granted, and problems if any between the family members in the business are pushed under the carpet, or postponed for future consideration, because business pressures on a day to day basis leave no time for attending to such issues.

So long as the business grows, and wealth accumulation is possible, with cash flows being good, ‘business is as usual’. But, below the surface, individual feelings do get bottled up. Even then, if the enterprise continues to be with the members of a single family, not much damage may be caused over the next few years.

The real issues begin to emerge with the growth and extension of the family with marriages, children, and concurrent increase in responsibility and commitment of each son or brother to their respective families. Internal pressures are now ready to take off.

Pressures become more serious where the patriarch of the family has passed on.

Once all the sons or brothers are married and have their own families, the enterprise is no longer ‘single-family owned’ – it is now owned by more than one family with multiple vested interests in the business.

When the third generation is ready to enter the business, and the business has not grown adequately to service the increase in numbers of potentially business-active members of the ‘families’, bottled up issues can become explosive. And the business can almost reach breaking point unless damage control exercises are carried through till an acceptable solution emerges.

Part of the problem is that family-owned and managed enterprises have been inducting into the business – as a matter of ‘duty’ - new cost-incurring but profit-sharing family members at a rate higher than their business growth rate.

Each induction must necessarily result in value addition to the business. However, more new family members with higher standards of living but without concurrent value addition capability, dependent on a stagnant or slow-growth business, means greater chances of poor performance and sickness, and of conflict and stress.

There are many other issues confronting family enterprises today including induction of wives, daughters, daughters-in-law into the business, ‘leadership among equals’, and ‘professionalization’ both in terms of attitude, knowledge, and result-orientation of family managers, and in terms of inducting qualified ‘external to family’ professionals who will require to be handled with care.

The issues of keeping out female members of the Families in the management of the Family Business are largely because of traditional gender discrimination in a male-dominated business environment. However, in more liberal families in business, involvement of female members, particularly daughters, even if they are otherwise qualified, and capable, is dependent mainly on possible ‘Conflict of Interest’ arising from marriage.

When it comes to ‘Professionalization’, in many family enterprises, there is actually a reluctance to induct proven, intelligent professionals. The truth is that it is easier to enforce ‘Accountability for Performance’ with Professionals than with Family Managers. Good Professionals are a support to Family Business, not a threat, assuming, of course, the Core Values of a Family Business are headed towards positive enhancement and growth of the Family Business.

A large percentage of family enterprises, particularly the older ones, have continued to run their businesses internally with a feudal undercurrent that encourages subservience and consequent mediocrity in employee quality and performance standards.

Unfortunately, functioning in such an environment every day over the years can lead family managers to attribute to themselves an exaggerated estimate of their own knowledge and performance capacities. This tends to be tested often in the tough market and the external world much to the disadvantage of the family enterprise.

The other very important issue is ‘Succession’, which is really one very significant part of the ‘planning for change’ process.

If ‘Money’ and ‘Wealth’ are not serious issues, and this is so in some of the older family enterprises, it is the desire for ‘Power’ that vitiates the family business environment, and complicates any effort at achieving ‘Fair Succession’. The struggle for Power, and concurrent Nepotism, with the absence of Accountability, together form a lethal mix that prevents merit-based Succession.

The 'Power Struggle' becomes even more vicious in a stagnant business situation. Also promotes situations of 'Conflict of Interest' as relationships take a toss.

'Letting Go' has become a somewhat serious and ironical problem particularly in recent years as older generations are fitter in their late sixties, and in their seventies, even while younger generations aspire for greater responsibilities in their thirties and forties.

In many cases, 'Letting Go' to ease 'Succession' can be facilitated by an attractive and productive Retirement Policy where the 'Elder' will continue to enjoy certain perks of higher management, but without direct and actual operational or strategic responsibility, that will support one's social and economic status in one's relevant social and business circles and community.

There is a misconception in the minds of members of some Family Businesses that having a 'Family Constitution' will solve all their problems. The reality is that a Family Constitution, in whatever nomenclature, evolves, and functions effectively only when the key members of a Family Business have a strong desire to be together in the long term. If the basic will to stay together is weak, and conflicts are particularly about money and wealth, a Family Constitution will be nothing but a short term cover-up destined to fail.

It is somewhat inevitable that being confronted by the seriousness of issues in achieving 'Growth with Harmony', in an obviously very competitive business environment, family-owned-and-managed enterprises, have to rapidly multiply the process of change….in the following directions:

1. Family Enterprises need to plan for their future. Sounds obvious but is missing even among 'modern and educated' members of Family Enterprises. I have more than once been surprised how easily 'MBAs' in the younger generation begin to enjoy the comfort of 'walking in' to a position of power (and perks) without accountability to deliver on performance, and also enjoying 'Nepotistic' protection!

2. Family Enterprises need to 'formalize' their management structure of business-active family members/ partners/ directors of the enterprise in terms of role definition, functional responsibility, authority, reporting, accountability

and performance appraisal, and the reward system. Again, obvious but missing more than one expects……

3. Family Enterprises need to match the enterprise/business purpose, objectives and plans with the requirements both of the incoming younger generation as also of the existing partners to be able to cope with increasing complexities of running the family business in particular, and of business in general.

4. Family Enterprises need to evolve a ‘Management Procedure and Code of Conduct’ package, with external assistance if necessary, that could evolve into a ‘Partnership Pact’ or a ‘Governance Code’ or a ‘Family Constitution’ or a ‘Family Protocol’ to sustain Unity during and after the change process on a long-term basis:

- as the Family Business grows, across many locations,
- and also as the number of Family Members in Business increases to a level where traditional and frequent face-to-face interpersonal contact is no longer possible

5. ‘Succession’ as a process must not be translated into over-simplified Nepotism or a whimsical exercise in which a dominant family member forces a wrong decision deliberately overlooking merit, and the others have to go along to maintain the peace. In fact a good ‘Succession Plan’ will re-structure the enterprise to harness the leadership skills and potential of competent members of the family, and therefore help create new growth opportunities that will further enhance opportunities for progress of other family members, and of the family enterprise group.

6. Tax Planning as part of a Restructuring Strategy, consequent to Succession Planning, is necessary and important. However, Tax Planning must not over-ride the need to sustain Family Business Unity into future generations. To re-emphasize, being obsessed with sustaining Family Business Unity is more precious than saving Tax as the primary motivation in restructuring for ‘Unity with Growth’.

7. Distrust within a Family Business/ Family Business Group multiplies proportionately to increase in scale of unaccounted business transactions, and in increased incidence of 'Conflict of Interest', as the number of Family Members in Business increase, within such a Family Business culture that may have existed over time.

8. In most cases, feelings of financial and social insecurity among either less advantaged or less competent family members, and of aging family members, in the enterprise, can result in ego clashes, lack of trust, destructive nepotism, and other obstacles to survival of the family business. To a very large extent this can be pre-empted by establishing family-constituted and professional advise assisted entities driven by a Family Constitution to ensure a process of common wealth management, of ensuring minimum economic support, of protection from unforeseen disasters and calamities, and of providing personal and social security into old age.

8.1. The 'Family Office' can be the facilitator and administrator of this process of ensuring family well-being, and of peace within the family.

8.2. Such a process, if properly planned and constituted, can promote Meritocracy as the key driver as far as the Business part of the family is concerned since less competent family members are taken care of otherwise, through the Family Office.

9. Conclusion: I am not 'Spiritual' in my approach to problem solving.......I have been profoundly influenced by the 'Logic of Business' in general, and of the Family Dynamics that influence Family Business, in particular. I do believe, and I do promote, certain *'Core Values of Family Business'*...... **Trust, Integrity, Ethics, Relationships, Reputation, Results, Accountability.....TIERRRA….**Now if these Values, as a whole, correspond to content of 'Spiritual' books and teachings, I would just claim to be blessed by coincidence......I make no effort to quote from them......

.**9.1. It is finally the 'Business' that will provide the resources for building family security and wealth, and of wellbeing, and of peace. Therefore, Business has to be Governed, Strategized and Structured to grow profitably in perpetuity. So there is peace in the 'Family'.**

9.2. Growth is the greatest driver, Stagnation the greatest enemy.

9.3. Growth supports and perpetuates Unity, always.

Family Businesses by their very nature are entrepreneurial. They are necessary constituents of a dynamic society riding on a new economic wave. I will not be exaggerating when I say that India – minus the passing hiccups - continues to be in the process of emerging into a spanking new entrepreneurial society where, paradoxically, it will be even more difficult to survive, if you have ***not*** done your homework, but if you do your homework, then it could be NIRVANA all the way!

Many family enterprises across the country have already initiated the change process. There are also many examples today to prove that in an unsuppressed creative business environment, a flood of successful first-generation entrepreneurs is emerging with a multiplier effect.

The horizon of opportunity has widened like never before, truly into a "borderless world". Family enterprises need to recognize this fact and initiate the change process. They have little choice, for markets do not wait. It is *always* a race against time.

PROMAG CONSULTANCY SERVICES **Raju Swamy/ November 05, 2018**

Raju Swamy
Founder
& Advisor to Family Business
PROMAG Consultancy Services
Bangalore - 560004 INDIA
Tel. +91-80-26676298/ Cell: 9845271498
Email: rajupromag@hotmail.com
www.promagconsult.in